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IN THE

Supreme Court of the United States

OCTOBER TERM 1962.

No. 553

ASSOCIATED TELEPHONE AND TELEGRAPH COMPANY,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

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1. The issue herein is of substantial and continuing significance. Respondent's argument in its Brief in Opposition ("Br. Opp." p. 7ff.) to the contrary is invalid.

Respondent, as the basis of its argument, purports to quote (Br. Opp. p. 7, n. 4) the "relevant" portions of §15 of the Revenue Act of 1962, P. L. 87-834, 76 Stat. 960 (the "1962 Act"), which added new §1248 to the Internal Revenue Code of 1954 (the "1954 Code"). Respondent, however, fails to quote or even refer to subsection (d)(3)*

* Section 1248(d)(3) provides in pertinent part:

"(d) EXCLUSIONS FROM EARNINGS AND PROFITS. For purposes of this section, the following amounts shall be excluded, with respect to any United States person, from the earnings and profits of a foreign corporation:

* * * * *

"(3) LESS DEVELOPED COUNTRY CORPORATIONS. Earnings and profits accumulated by a foreign corporation while

of §1248 which clearly is relevant and expressly excludes accumulated earnings of "less developed country corporations"* from the special tax computation rules of such section. Thus, contrary to Respondent's contention, the issue herein has very substantial and continuing significance with respect to liquidating dividends from post-1962 earnings and profits distributed by "less developed country corporations"—which may well include foreign subsidiary corporations doing business in Central and South America, Asia, Africa, portions of Europe and possessions of the United States.

Resolution of the issue by this Court is actually now more important than before the 1962 Act. The foreign tax rates in "less developed countries" are *generally lower* than the United States capital gain rate. Hence, a serious question is now presented as to the applicability after 1962 of the decisions below and in *Fowler Hosiery Co., Inc.* v. *Comm'r*, 301 F. 2d 394 (7th Cir. 1962) which were largely predicated upon the assumption that the foreign tax rates involved would be *generally higher* than the United States capital gain rate.

The continuing capital gain treatment provided under the 1962 Act for the liquidation of "less developed country

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it was a less developed country corporation (as defined in section 902(d)), if the stock sold or exchanged was owned for a continuous period of at least 10 years, ending with the date of the sale or exchange, by the United States person who sold or exchanged such stock."

See also S. Rep. No. 1881, 87th Cong., 2d Sess. (1962).

* A "less developed country corporation" is defined in §§902(d) and 955(c)(1) of the 1954 Code, generally, as a foreign corporation doing business in a "less developed country." A "less developed country" is defined for this purpose in §955(c)(3) of the 1954 Code as any foreign country (outside the Sino-Soviet Bloc) or United States possession so designated from time to time by Executive Order of the President with the exception of 21 countries specified therein.

corporations" (whether the gain be attributable to earnings and profits accumulated before, during or after 1962) was obviously designed to encourage the establishment and extension of subsidiary operations in the underdeveloped areas of the world. It would be contrary to such Congressional policy to require double international taxation of such subsidiaries' earnings (through denial of any foreign tax credit under §§901 and 902 of the 1954 Code) merely because they are remitted to the United States in the form of liquidating dividends and thereby qualify for the intended capital gain relief. Frequently economic and political changes in less developed countries leave no choice but liquidation of such subsidiaries.

Furthermore, §1248 has no application whatever to earnings accumulated prior to 1963 regardless of where the foreign corporation is engaged in business, when it is liquidated, or how long its stock was owned.

In any event, §1248* makes no reference to foreign tax credits generally, or to §902 in particular. The Senate Finance Committee Report (S. Rep. No. 1881, 87th Cong., 2d Sess. 300 (1962), quoted by Respondent at Br. Opp. p. 9) as well as the House Ways and Means Committee Report (H. R. Rep. No. 1447, 87th Cong., 2d Sess. A124 (1962)) expresses no opinion as to the applicability of the foreign tax credit "provided by the code without regard to new section 1248" except to indicate that there is no foreign tax credit with respect to "the portion of the gain

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* Section 1248 was added to Part IV of Subchapter P of Chapter 1 of the 1954 Code, relating to "SPECIAL RULES FOR DETERMINING CAPITAL GAINS AND LOSSES", and merely provides special tax computation rules whereby long-term capital gains realized on the sale or exchange of stock in certain foreign corporations (except "less developed country corporations") are taxed at ordinary income rates to the extent of post-1962 earnings and profits.

that is not a dividend". The 1962 Act Committee Reports thus leave open the question of whether a distribution of accumulated earnings in partial or complete liquidation is a "dividend" within the meaning of §902(a) in the absence of the special tax computation rules of §1248. This is the very issue which should be resolved by this Court.

Moreover, this Court has indicated that any observation or implication in a Congressional committee report *issued many years subsequent to the enactment of the original section in question* (§238(e) of the Revenue Act of 1921, c. 136, 42 Stat. 227) is entitled to no weight.*

2. Respondent relies upon some general language in *Hellmich* v. *Hellman*, 276 U. S. 233 (1928), in a context completely different from that in the instant case, for Respondent's view that the term "dividends" can never include a distribution of earnings and profits in liquidation. (See Br. Opp. p. 5.) The Respondent similarly relied upon the *Hellman* case in the Court below, but such argument was rejected.** The *Hellman* case involved the taxability to an individual shareholder of liquidating distributions under the Revenue Act of 1918, c. 18, 40 Stat. 1057; and this Court

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* See *Penn Mutual Life Ins. Co.* v. *Lederer*, 252 U. S. 523 (1920) in which Justice Brandeis stated:

> "But no aid could possibly be derived from the legislative history of another act passed nearly six years after the one in question. Further answer to the argument based on the legislative history of the later act would, therefore, be inappropriate." 252 U. S. at 538.

See also *U. S.* v. *Wise*, 370 U. S. 405 (1962). This principle was recognized by the Court below in the instant case (see Petition, Appendix B, pp. 10-11), as well as in *Fire Companies Bldg. Corp.* v. *Comm'r*, 54 F. 2d 488, 489 (2d Cir. 1931), *cert. denied*, 286 U. S. 546 (1932). Such principle is also applicable to the observation of the House Ways and Means Committee in 1950, referred to in Br. Opp. p. 6, n. 3.

** See Petition, Appendix B, pp. 10, 16.

held that under the *express terms* of §201(c) of such Act, liquidating distributions were *taxable* as "other gains or profits" and, accordingly, could not qualify for the "dividends received" deduction allowed under §216(a) of such Act. Moreover, the most recent expression of opinion by this Court (*Comm'r* v. *Est. of Bedford*, 325 U. S. 283, 291, 292 (1945))—*that the general definition of "dividend" in §316(a) of the 1954 Code is applicable to the entire income tax subtitle*—is controlling herein in the absence of any language qualifying the term "dividends" as used in §902(a) of the 1954 Code. (See Petition, pp. 7, 8.)

In further support of its *Hellman* argument, Respondent indicates that under §331 of the 1954 Code, liquidating distributions "have tax consequences completely different from those attaching to dividends." (Br. Opp. p. 6.) This simply means that by reason of §331 liquidating dividends are taxable at capital gain rates. There is no language in §§316(a), 331(a) or any other statutory provision which excludes liquidating dividends from the meaning of the term "dividends" as used in other contexts in the 1954 Code such as the foreign tax credit provisions. While the Respondent recognizes that the purpose of §902(a) "is to avoid double taxation," citing *American Chicle Co.* v. *U. S.*, 316 U. S. 450 (1942) (Br. Opp. p. 7), he disregards the point basic to this issue, *viz.*, that the lower court decisions, which were based upon tax rate differentials, result in the very type of international double taxation of income which the foreign tax credit provisions (as well as the income tax conventions with foreign countries) are designed to prevent.

3. Although, as Respondent recognizes (Br. Opp. p. 6), there is conflict in reasoning among the lower courts on this issue, Respondent does not dispute that all of such deci-

sions rest primarily upon a comparison of foreign tax rates and the United States capital gain rate on a *particular item* of income. Such decisions, therefore, are completely inconsistent with the pattern of the statutory limitation on foreign tax credits contained in §904 of the 1954 Code.* (See Petition pp. 9-11.)

Respectfully submitted,

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* It was not until the enactment of §10 of the 1962 Act (adding new subsection (f) to §904 of the 1954 Code) that the Congress required a separate foreign tax credit limitation based upon a *particular item* of income, *viz.*, certain interest income derived from foreign sources. As is apparent from the Senate Finance Committee Report (S. Rep. No. 1881, 87th Cong., 2d Sess. 72 ff.) the Congress understood perfectly well that hitherto there was no separate limitation in the foreign tax credit provisions based upon the rates of tax applicable to specific types of income (whether taxed at capital gain rates or otherwise).